

# Prop. 26 – New Limits on Government Fees

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# MICHAEL G. COLANTUONO

## Colantuono & Levin, PC

11364 Pleasant Valley Road  
Penn Valley, CA 95946-9000

(530) 432-7359 (voice)

(213) 542-5739 (voice)

(530) 432-7356 (fax)

[MColantuono@CLLAW.US](mailto:MColantuono@CLLAW.US)

[WWW.CLLAW.US](http://WWW.CLLAW.US)

Twitter: @MColantuono; Linked-In: Michael Colantuono

# Proposition 26 – Overview

- Proponents' goal was to repeal *Sinclair Paint Co. v. State Bd. of Equalization* and make it more difficult for gov'ts to enact fees
- Specific target: Regulatory fees
- Reclassifies many “fees” as “taxes”
- Reiterates that gov't has the burden to prove a fee or charge is not a tax

# Impact on State Government

What is a state “tax” under Prop 26?

- “Any levy, charge, or exaction of any kind imposed by the State”
- Unless it falls under one of five exceptions or is not “imposed”
- Overall effect: Legislature must now pass most charges that were formerly “fees” by 2/3<sup>rds</sup> vote because they are now “taxes”

# Changes in Approval Requirements

<b>Taxes</b>	<b>Exceptions (any charge other than a tax)</b>
A 2/3 <sup>rds</sup> majority of each house of the Legislature or constitutional initiative approved by a simple majority of voters (Prop. 13)	Majority of each house of the Legislature

# Impact on State Government

Programs funded by fees that would likely require a 2/3<sup>rds</sup> vote if adopted after 1/1/10:

- California Used Oil Recycling Fund
- Underground Storage Tank Cleanup Fund
- Pesticide Regulation Fund
- Air Pollution Control Fund
- Oil Spill Administration Fund

# 1: Exception for Benefits & Privileges

A charge imposed for a **specific benefit conferred or privilege granted** directly to the payor

1. Not provided to those not charged
2. Doesn't exceed reasonable costs to the gov't of conferring the benefit or granting the privilege to the payor

E.g., professional & ABC licenses, franchises

## 2: Exception for Services & Products

A charge imposed for a **specific government service or product** provided directly to the payor

1. Not provided to those not charged
2. Doesn't exceed reasonable costs to government of providing service / product

E.g., park services, medical services

Issue: free or discounted services / products



## 3: Exception for Regulatory Costs

A charge imposed for **reasonable regulatory costs** to the government incident to

1. Issuing licenses and permits
2. Performing investigations, inspections & audits
3. Admin. enforcement and adjudication

Issues:

- Unclear how this different from 1<sup>st</sup> exception
- Unclear if this covers rulemaking and other general administrative costs

## 4: Exception for Use of Gov't Property

A charge imposed for

1. **Entrance to or use of gov't property**
2. **Or purchase, rental, or lease of gov't property**
3. As to state, doesn't cover Vehicle License Fees

E.g., park entrance and equipment rental fees

Issue: No reasonable cost limitation; compare burden-shifting language

## 5: Exception for Fines & Penalties

**A fine, penalty, or other monetary charge**

1. Imposed by the judicial branch of government or the State or a local gov't
2. As a result of a **violation of law**

E.g., criminal fines, parking fines, late penalties

## More on Fines & Penalties

- **Cal. Tax v. FTB (2010) 190 C.A.4<sup>th</sup> 1139**
  - 20% penalty on late corporate taxes raising \$1.4b was not a tax
  - Distinguishing characteristics: label, revenues diminish overtime, triggered by violation
  - No need for findings, good faith defense; post-payment remedy sufficient

# Revenue Neutral Laws

- Previously, Legislature arguably could raise a tax w/out 2/3 vote if it lowered another tax by the same amount because Prop. 13 applied to laws that **“increased revenues”**
- Now, any laws that **“result in any taxpayer paying higher tax”** must be approved by a 2/3<sup>rds</sup> majority
- For example, the “gas tax swap”

# Retroactivity

- Prop. 26 explicitly “voids” State taxes adopted after 1/1/10 unless readopted by 11/3/11
- No analogous provision for local laws
- Potential examples:
  - Gas tax swap – Legislature readopted by 2/3 vote in 2011
  - AB 2398 – carpet waste reduction fee
  - AB 1343 – paint recovery fee

## Retroactivity & AB 32

What about AB 32 (Global Warming Solutions Act of 2006)?

- Legislature adopted AB 32 in 2006
- Health & Safety Code § 38597 gives California Air Resources Board authority to impose fees on greenhouse gas emitters
- CARB adopted “Cost of Implementation” fees 9/25/09; OAL approved regulation 6/17/10

## Retroactivity & AB 32

- Does Prop. 26 repeal the Cost of Implementation regulation?
- Does Prop. 26 require a 2/3<sup>rds</sup> vote for future regulations imposing fees?
- Probably not: § 1(a) applies to any change in “**state statute**” that results in higher taxes
- Similarly, the retroactivity provisions of §3(C) state any tax adopted after 1/1/10 must be “**reenacted by the Legislature**”



## Other Issues

- Changes that indirectly result in a taxpayer paying higher taxes
  - increasing the minimum wage
- Inflation adjustments & other automatic increases
  - Gov't Code § 53750(h)(2)(A) exempts automatic inflation adjustments, but applies only to local gov'ts
  - However, 2/3<sup>rd</sup>s vote not necessary if adjustment does not require a change in "state statute"

## Still More Issues

- Unfunded mandates
  - Under the provisions affecting local governments, more funding measures will be subject to voter approval
  - A mandate is “unfunded” if the local agency needs voter approval to fund program

## Conclusion as to State

- State fees not falling under any of 5 exceptions are now taxes subject to 2/3<sup>rds</sup> vote requirement
- Some fees may fall w/in 2 or more exceptions
- Will have significant impact on funding of State environmental, public health, and social programs
- Fees passed before 1/1/10 grandfathered

# Local Government Perspective

- Most of what has been said about State also applies to local government but:
  - No retroactivity (protects all existing legislation, including implementation)
  - Much clearer interpretive rules b/c 26 amends Prop. 218, so Prop. 218 & Omnibus Implementation Act (GC 53750 ff.) apply; *cf. Greene v. Marin Co. Flood Control & Water Cons. Dist.* (2010) 49 Cal.4<sup>th</sup> 277

# Exceptions Limited to Cost of Service or Regulation

- Specific Benefit / Privilege (permits, franchises)
- Specific Service / Product (utility charges, park & rec. fees)
- Reasonable Regulatory Fees for licenses & permits (permits, inspections)

# Prop. 26 Exceptions Not limited to Cost Recovery

- Fee for entry, use or purchase of gov't property (park & rec. entrance fees, equipment rental, franchises)
- Fines & penalties

# Prop. 26 Exceptions Specific to Local Gov't

- Fees imposed as a condition of property development (limited to cost by AB 1600, Gov't Code § 66000 et seq., and other law)
- Assessments & property-related fees subject to Prop. 218 (limited to cost by 218)

# Language discrepancies between State & local provisions

- Exceptions for benefits / privileges & services / products: State provision ends w/ providing or granting “to the payor.”
- Exception for reasonable regulatory costs – state version refers to costs “incident to issuing licenses and permits;” local says “for issuing ...”



## Another oddity

- Exceptions for reasonable regulatory costs for both State and local governments reference “agricultural marketing orders”
  - Local governments do not enforce such orders

# Definitional issue

- State & local provisions define as taxes “any levy, charge, or exaction ... **imposed** ...”
  - What does “imposed” mean?
    - **Ponderosa Homes v. City of San Ramon** (1994) 23 Cal.App.4th 1761, 1770 (dictionary definition suggests force or authority required)
  - Can we exclude:
    - voluntary payments?
    - prices set in competition w/ non-gov’t providers?

## Another Definitional Issue

- Exceptions refer only to “charges,” but seem to have same breadth as “levy, charge or exaction”
- Limiting exceptions to “charges” would make them nearly moot
- *Cf. Bighorn-Desert View Water Agency v. Verjil* (2006) 39 Cal.4<sup>th</sup> 205 (“fee” and “charge” synonymous under Prop. 218)

# Burden of Proof

- Gov't bears burden to prove by preponderance:
  - Not a tax
  - Fee amount doesn't exceed cost
  - Cost allocation reasonably related to payor's benefits from / burdens on gov't activity
- Burden of Production, too:
  - *Homebuilders Ass'n v. Lemoore* (2010) 185 Cal.App.4<sup>th</sup> 554

## More on Burden of Proof

- Doesn't impose cost limit on exceptions 4 – 7
  - When other law imposes cost limit on a fee, gov't bears burden of proof, but this is not an independent source of a duty to limit fees to cost
- Gov't can choose whether to use benefit or burden justification under *Sinclair Paint* line of cases from which this test is drawn

# Major Impacts on Local Gov't

- Gas & Electric Utilities
- Non-property-based assessments
- Park & Rec. service fees? *Cf.* Gov't Code § 50402
- Discounts & free passes for fees excepted as benefit / privilege or service / product
- Scope of recoverable regulatory costs
- Application to voluntary payments (development agreements, *e.g.*)
- In-lieu fees

## More Impacts of Prop. 26

- Gas & electric rates exempt from 218; not 26
  - General fund transfers now problematic
  - But Prop. 26 is not retroactive
- Some good news for some local governments at expense of other agencies:
  - Fish & Game Fees
  - Booking Fees
  - Property Tax Administration Fees

# Prop. 26 Litigation

- Citizens for Fair REU Rates v. City of Redding (Shasta CSC filed 2/11/11)
  - Does PILOT from electric utility violate Prop. 26 when rates, but not PILOT increased post-26?
- Ventura v. United Water Conservation Dist. (Ventura CSC filed 08/11)
  - Challenge to 3:1 ratio of agricultural to M&I groundwater charges under Props. 218 & 26



# More Prop. 26 Litigation

- Schmeer v. County of Los Angeles (LASC filed 10/3/11)
  - Does \$0.10 fee on paper bags collected by retailers under County plastic bag ban violate 26?

## Prop. 26 To-Do's

- Protect grandfathered fees / fee components
- Be careful when adopting or increasing fees
- Review existing fees
- Considering segregating discretionary from non-discretionary fee proceeds
- Consider fees by agreement rather than by ordinance or rule
- Stay tuned!

# Questions?

